

**Katten Financial Markets and Funds Quick Take**

June 2022

**Regulatory Alert! A Joint Audit Committee Reminder to FCM Legal and Compliance Personnel**

The Joint Audit Committee (JAC) is a club of futures exchanges, in their capacities as self-regulatory organizations (SROs). Under a delegation of authority from the Commodity Futures Trading Commission (CFTC), the JAC monitors and examines member futures commission merchants (FCMs) for compliance with financial, reporting and risk management requirements (including rules relating to segregation of customer funds) adopted by member SROs and the CFTC. The JAC has issued a Regulatory Alert, 22-02, reminding member FCMs of their obligations under CFTC Regulation 1.11. It's safe to infer that the Alert is based on compliance gaps detected in recent FCM regulatory exams by member SROs.

CFTC Regulation 1.11 requires an FCM to establish, maintain and enforce a system of risk management policies and procedures designed to monitor and manage the risks associated with the activities of the FCM. JAC Alert 22-02 identifies several requirements that FCM Legal and Compliance personnel will want to confirm are adequately addressed in reviewing their Regulation 1.11 Risk Management Programs. [Read about the requirements included in JAC Alert 22-02.](#)

**SEC Proposes Rules Concerning Investment Adviser and Investment Company ESG Disclosure**

On May 25, the Securities and Exchange Commission (SEC) proposed amendments to various rules relating to fund and advisers incorporating environmental, social and governance (ESG) factors in disclosure. The proposed amendments seek to categorize certain types of ESG strategies broadly and require funds and advisers to provide more specific disclosures in prospectuses, annual reports and adviser brochures based on the ESG strategies they pursue. For example, a fund that seeks to achieve an ESG-related objective would be required to disclose how it measures progress toward that objective. If adopted, the amendments would apply to certain registered investment advisers, advisers exempt from registration, registered investment companies and business development companies.

The comment period for the proposed amendments will remain open for 60 days after publication in the *Federal Register*. [Read about the SEC's proposal.](#)

**SEC Proposes Changes to Investment Company Act "Names Rule"**

The SEC has proposed amendments to Rule 35d-1 under the Investment Company Act of 1940 (the "names rule"). The names rule currently requires a registered investment

company or business development company (BDC) whose name suggests either a focus on a specific type of investment, a focus in investments in a specific industry or a geographic focus, to adopt a policy to invest at least 80 percent of the value of its assets in those investments suggested by its name.

The amendments propose to, among other things: (i) expand the 80 percent investment policy requirement to apply to any registered investment company or BDC name with terms suggesting that the fund focuses in investments that have, or investments whose issuers have, particular characteristics (including, for example, "growth" or "value"); (ii) narrow the circumstances in which a registered investment company or BDC is permitted to depart from its 80 percent investment policy; (iii) require that any unlisted registered investment company or BDC obtain a shareholder vote before changing its 80 percent investment policy; (iv) impose specific guidelines on the use of environmental, social and governance (ESG) terms in registered investment company or BDC names; and (v) implement related reporting, notice and recordkeeping requirements. [Read about the names rule.](#)

### **FINRA Proposes Changes to Enhance TRACE Reporting Obligations**

The Financial Industry Regulatory Authority, Inc. (FINRA) filed with the Securities and Exchange Commission (SEC) a proposed rule change to amend FINRA Rule 6730 to:

- (i) require members to report electronically executed transactions in US Treasury Securities to FINRA's Trade Reporting and Compliance Engine (TRACE) in the finest increment captured by the system used to execute the transaction, subject to an exception for members with limited trading volume in US Treasury Securities; and
- (ii) reduce the trade reporting timeframe for transactions in US Treasury Securities to generally require reporting to TRACE as soon as practicable but no later than 60 minutes.

[Read FINRA's proposed rule change.](#)

### **CME Derived Blocks – A New Way to Price Block Trades on Certain CME and CBOT Security Index Futures**

On May 23, the Chicago Mercantile Exchange (CME) implemented new functionality under its block trade rule permitting dealers to trade "derived blocks" in certain equity index futures contracts. A derived block trade is a block trade the price and quantity of which depends on hedging transactions by the dealer that take place after the block trade has been agreed, but prior to its being submitted to the exchange. Derived block trades are available solely in CME E-mini Select Sector futures and CBOT Dow Jones US Real Estate Index futures, at the existing block trade minimum thresholds applicable to those contracts. [Read about the CME's derived blocks functionality.](#)

### **The LME's Consultation on OTC Position Reporting**

The London Metal Exchange (LME) announced a consultation with members on a proposal to require reporting of all "over-the-counter (OTC) positions" in certain physically deliverable metal contracts. The proposal was prompted in response to a spike in nickel prices on March 8 when the LME suspended trading in all nickel contracts (which did not resume until March 16) and cancelled all trades executed after midnight on that day. The LME's "independent review" into those events and their aftermath is ongoing (as are regulatory reviews by the Financial Conduct Authority (FCA) and the Bank of England), but the exchange has already identified one salient contributory factor: "sizable positions in the OTC market and the LME's lack of direct visibility of such activity."

Under the proposal, members would be required to submit, on a weekly basis, details of all OTC positions (that is, positions in LME contracts not cleared by LME Clear) in aluminum and aluminum alloy, cobalt, copper, lead, nickel, tin and zinc, including all OTC contracts that are financially settled against an LME reference price or physically deliverable with LME warrants or warehouse receipts. OTC baskets and index trades referencing the specified LME contracts would also be reportable where the LME constituents represent at least 20 percent of the underlying. No minimum threshold would apply; all positions, regardless of size, would be reportable. [Read about LME consultation.](#)

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## CONTACTS

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